

General Information Letter: Alternative apportionment petition cannot be granted when it evidences a misunderstanding of the statutory apportionment formula.

June 9, 2003

Dear:

This is in response to your correspondence and Petition dated May 12, 2003. Department of Revenue ("Department") regulations require that the Department issue only two types of letter rulings, Private Letter Rulings ("PLRs") and General Information Letters ("GILs"). PLRs are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. GILs do not constitute statements of agency policy that apply, interpret or prescribe the tax laws and are not binding on the Department. For your general information, the regulation governing the issuance of letter rulings, **2 Ill. Adm. Code Part 1200** regarding rulings and other information issued by the Department, can be accessed at the Department's website. That address is www.revenue.state.il.us/legalinformation/regs/part1200.

Although you have requested a ruling granting an alternative allocation or apportionment, because the Petition fails to sustain the burden of proof required pursuant to **86 Ill. Adm. Code 100.3390**, the Department feels that it is appropriate to respond by GIL.

In your correspondence, you state as follows:

Facts:

- COMPANY LLC ("The Company") is incorporated in Delaware and is qualified to do business, and has its only office and employees, in the State of New Jersey. The Company is a limited liability company taxed as a partnership.
- Starting in 2002, most of the Company's small amount of inventory was maintained in and shipped from a public warehouse in Illinois. This is the only basis for the Company having nexus in Illinois.
- All property (except for the inventory in the warehouse), rent and salaries are in New Jersey.
- All sales are generated by an executive located in New Jersey.
- At the request of the Company's significant customer (which is headquartered in New Jersey), the majority of the Company's sales pass title to that customer upon delivery from the Illinois warehouse. Therefore, according to Illinois regulations, these sales are Illinois source income. While title passes in Illinois, over 95% of the sales to this customer are then sent to the customer's U.S. stores not located in Illinois. Note that the Company's customers are willing to let title pass in the future at the locations where the products are shipped if the Company requests, in which case the allocations of income to Illinois would be minimal.
- Illinois' standard business income apportionment formula is a one-factor formula utilizing sales.
- New Jersey's standard business income apportionment formula is a three-factor formula utilizing sales, property and salaries.

Results:

Utilizing the standard apportionment formulas for each state results in approximately 95% of the net income allocated to Illinois and approximately 68% allocated to New Jersey. Therefore, the Company would have to pay tax on approximately 163% of its net income. This result does not fairly represent the Company's business activity in Illinois. The majority of the Company's business activity is taking place in New Jersey. The production of the inventory (and its cost) is allocable to 2002. The sale of this specific product occurred in 2002 and will continue in the future indefinitely, hopefully in greater volume.

Request:

Since the actual business activity in Illinois is very small, the Company hereby requests, beginning in 2002, the use of a three-factor formula for Illinois income tax purposes. The formula would allocate property (including inventory), payroll and sales within and without Illinois. In addition, it is requested that only 50% of the sales currently allocable to Illinois are included in Illinois sales to properly reflect the effort taken in New Jersey to generate these sales. Based on 2002 results, the allocation to Illinois would be approximately 21%.

The Department believes that it may be premature to rule on the merits of your Petition. As you have correctly pointed out, Illinois currently employs a single sales-factor method for apportioning business income. Illinois Income Tax Act Section 304 (h), 35 ILCS 5/304(h) (2003). Regulations promulgated under this statute provide as follows:

c) Numerator. The numerator of the sales factor shall include the gross receipts attributable to this State and derived by the person from transactions and activity in the regular course of its trade or business. All interest income, service charges, carrying charges, or time-price differential charges incidental to such gross receipts shall be included regardless of the place where the accompanying records are maintained or the location of the contract or other evidence of indebtedness.

1) Sales of tangible personal property in this State.

A) Gross receipts from the sale of tangible personal property (except sales to the United State Government) (see 86 Ill. Adm. Code 100.3370(c)(2)) are in this State:

i) if the property is delivered or shipped to a purchaser within this State regardless of the f.o.b. point or other conditions of sale; or

ii) if the property is shipped from an office, store, warehouse, factory or other place of storage in this State and the taxpayer is not taxable in the state of the purchaser...

Taking into account the rule stated above, it occurs to the Department that you may be overstating the amount of sales which should be attributed to this State by including their gross receipts in the numerator of the single-sales factor. If 95% of your sales involve goods shipped from an Illinois warehouse to points outside Illinois, it may be that as little as 5% thereof may be attributable here. We suggest that you review the destination point of your sales for 2002 in light of the rule set forth at

86 Ill. Adm. Code 100.3370 (c). It may obviate the need for a Petition For Alternative Apportionment.

As stated above, this is a GIL which does not constitute a statement of policy that applies, interprets or prescribes the tax laws, and it is not binding on the Department. If you wish to obtain a PLR which will bind the Department with respect to the application of the law to specific facts, please submit a request conforming to the requirements of **2 Ill. Adm. Code Part 1200** and **86 Ill. Adm. Code 100.3390**.

Sincerely yours,

Jackson E. Donley,
Senior Counsel-Income Tax